City of Detroit
CITY COUNCIL

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TO: COUNCILMEMBERS

FROM: Irvin Corley, Jr., Director ICJ.

DATE: October 29, 2008

RE: Obsolete Property Rehabilitation Exemption Certificate for Fort Shelby Hotel Project **(Recommend Approval)**

This report is for the 10:15 a.m. scheduled discussion today in the Planning and Economic Development Standing Committee on the Fort Street Hotel, LLC (petitioner) request for an obsolete property rehabilitation exemption certificate for the Fort Street Hotel project.

Delay in Obsolete Property Rehabilitation Exemption Certificate Request

Your Honorably Body approved the establishment of the obsolete property rehabilitation district for the Fort Shelby Hotel project in January 2003. The almost six-year delay in the request for Council's approval of the obsolete property rehabilitation exemption certificate is primarily due to the time it has taken to move the project along through various stages.

The stages include obtaining approval of financing from the City's General Retirement System and the City/HUD via the Section 108 loan program; transferring ownership of the Fort Shelby Hotel property from The Shelby Hotel, Inc. to MCP Development, LLC to Fort Shelby Holding Company, LLC over a two-year period; establishing subsidiaries (Fort Shelby Hotel, LLC and Fort Shelby Residential, LLC) for the syndication of federal and state tax credits and facilitation of the development process; and clearing up of minor glitches in the process of requesting for the obsolete property rehabilitation exemption certificate through the City.

Project Description

525-529 West Lafayette, a/k/a Condominium Unit 1, and commonly known as Fort Shelby Hotel represents a ten-story hotel that was originally built in 1918 with an addition added on in 1927. The hotel is approximately 343,000sf with retail, hotel rooms, ballrooms, and multi-level basements.

The Fort Shelby Hotel closed in 1975 and has become functionally obsolete through vacancy, inadequate floor design, and the need for extensive rehabilitation, including removal of asbestos, replacement of interior walls, mechanical, plumbing, electrical, HVAC systems and roof, and restructuring of floor plan to highest and best use.

The developer, Fort Shelby Hotel, LLC, plans to rehabilitate the property into a 204-room hotel from floors three through ten, with a ballroom, retail space, a lobby, bar/restaurant and back offices on the first floor; and 38,000sf of conference rooms, break room, and a repair/mechanical room on the second floor. Doubletree Guest Suites, the suite concept by Hilton Hotels, will be the hotel operator.

The developer anticipates hiring and retaining 300 full-time employees through out the life of the proposed 12-year abatement period. This is codified in an obsolete property rehabilitation exemption certificate agreement entered into between Fort Shelby Hotel, LLC and the Planning and Development Department. In addition, the project could generate over 300 construction jobs.

The developer is requesting for an obsolete property rehabilitation exemption certificate only for the hotel/retail portion. Time is of the essence for the certificate approval because the developer hopes to open the Fort Shelby Hotel during the month of December 2008.

For Council's information, the Fort Shelby project also comprises the development of 63 residential units with a mixture of one, two and three bedroom units on floors 11-21 and 1 penthouse unit with a terrace. The residential development is also commonly known as Condominium Unit 2. A subbasement will consist of 4,000sf of residential storage. Fort Shelby Residential, LLC will facilitate the residential development and may request for a NEZ district in the near future to facilitate this development.

L.S. Brinker Company, a Detroit headquartered minority-owned business, is the general contractor for project construction.

Downtown CDC Approval

Although not a requirement under the PA 146-Obsolete Property Rehabilitation legislation, for Council's edification, the Downtown Citizens' District Council acknowledged its approval of the Fort Shelby Hotel project, with the obsolete property rehabilitation district designation, in 2006.

Project Cost, Financing and Cash Flows

The developer, Fort Shelby Hotel, LLC, intends to spend approximately $63.9 million to rehab the Fort Shelby Hotel property. Eventually, Fort Shelby

Residential, LLC will spend $26.9 million to create the residential component. Consequently, total project cost could reach $90.8 million.

A sources and uses statement is attached supporting the total project cost with a breakdown of the hotel/retail and resident components of the project. Under the Sources section, the owners' equity, tax credit (federal and state historic and Michigan business tax) equity and Hilton capital contribution represent over 44% of the total project cost, which is very good. Owners' equity is primarily made up of a $13.3 million contribution in "conservation easement", which under IRS rules represents a tax credit for the donation of air rights/façade easement for the perpetual preservation of the historical integrity of the Fort Shelby property. The sale of the tax credit at 29 cents on the dollar generated this money. The Book Cadillac Hotel also received funds from this mechanism. Sources also include a $31.75 million loan from the General Retirement System and an $18.7 million Section 108 loan.

The project cash flows (which are available in our office for review) show the need for a 12-year obsolete property tax abatement in order to help the project generate sufficient cash flows to cover the various layers of debt service requirements and generate a reasonable return on investment for the developer. Without the abatement, the project becomes more marginal, since it will be a challenge for the developer to achieve reasonable hotel/residential occupancy rates in this dire economic climate that is predicted to last a while and tight credit markets.

Recommendation

Based on the above analysis, we recommend approval of a 12-year obsolete property rehabilitation exemption certificate for the 525-529 West Lafayette, Fort Shelby Hotel project.

Attachment

cc: Council Divisions
Auditor General's Office
Douglass Diggs, Planning and Development Department Director
Clinton Griffin, PDD Development Specialist
Joseph Harris, Chief Financial Officer
Pamela Scales, Budget Director
Londell Thomas, Mayor's Office

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Fort Shelby Hotel Redevelopment

Sources and Uses of Funds - STATIC MODEL

SOURCES OF CAPITAL

		TOTAL PROJECT	Residential Component	Hotel & Retail Component	Closing	C of O	PART III Approval
GRS 1st Mortgage Debt		24,000,000	6,900,000	17,100,000			
HUD 108 Loan		18,700,000		18,700,000			
					<<<<TIMING>>>>		
Tax Credit Equity							
Federal Historic	15,683,695				10,957,586	3,443,813	1,282,296
State	3,172,400						3,172,400
Single Business Tax	5,910,478					5,910,478	
		24,766,573	7,106,294	17,660,279			
Additional GRS 1st Mortgage Debt	2	7,750,000	1,333,163	6,416,837			
HILTON CAPITAL		750,000		750,000		750,000	
Owner's Equity (INCL CONSERVATION EASEMENT $$)		14,873,344	11,541,518	3,331,826			
TOTAL SOURCES OF CAPITAL		90,839,917	26,880,975	63,958,942			

USES OF CAPITAL

		TOTAL PROJECT	Residential Component	Hotel & Retail Component
ACQUISITION COSTS		7,177,685	3,747,224	3,430,461
HARD COSTS GMP	53,518,717		15,602,753	37,915,964
ARCHITECTURE & ENGINEERING COS	2,141,607	55,660,324	368,707	1,772,900
HARD COSTS OWNER		5,739,051	301,689	5,437,362
A&E OWNER (ADDITIONAL TO DESIGN/BUILD A & E)		459,710	130,816	328,894
LEGAL AND PROFESSIONAL COSTS		4,341,470	1,209,555	3,131,915
GENERAL AND ADMINISTRATIVE COSTS		981,287	287,015	694,272
LEASING AND MARKETING COSTS		390,000	390,000	0
HOTEL COSTS AND FEES		1,200,000	0	1,200,000
FINANCING AND INTEREST COSTS		2,610,913	955,253	1,655,660
GLOBAL EXETER FEE		1,560,448	806,643	753,805
OWNER'S CONTINGENCY COST		442,320	156,970	285,350
ADDITIONAL CAPITAL COSTS (Excl Interest)		7,803,982	2,220,708	5,583,274
TOTAL USES TO COMPLETE DEVELOPMENT		88,367,191	26,177,334	62,189,857
BRIDGE LOAN INTEREST - POST CONSTRUCTION (FUTURE TAX CREDITS REPAY)		2,472,726	703,641	1,769,085
TOTAL USES OF CAPITAL (INCL POST DEVELOPMENT)		90,839,916	26,880,975	63,958,942

INTEREST BREAKDOWN (THROUGH CONSTRUCTION)

HUD		763,411			
GRS		647,218			1,572,255
INT ON ADDT'L CAPITAL		-	INCL IN GRS INTEREST LINE		
SHORE		161,627			
OTHER FINANCING COSTS		1,038,658			
		2,610,913			

EQUITY COMPOSITION

MCP Equity		-		
Deferred Development Overhead		-		
Conservation Credits - Net of Global Exeter Fee		13,383,500	SEE BELOW	
GX CONTRIBUTION TO EASEMENT INSURANCE		-		
INTEREST INCOME	0	50,000		
INITIAL OWNERS EQUITY		1,429,844		PRIOR COSTS LEFT IN THE DEAL
SPECIAL EQUITY FOR S-CORP		10,000	1,439,844	
ADDITIONAL OWNERS EQUITY		0		
		14,873,344		

CONSERVATION EASEMENT

	$ 0.29		
Conservation Easement Value **Allocated To Chevron**		46,150,000	
Sale Price - Up Front		-	
Sale Price - Back End		13,383,500	Timing From Chevron Assumed To Be Month 52 From Closing
Global Exeter Fee		(539,000)	FEE BASED ON ASSUMED CAPITAL FROM CHEVRON (FEE PAID AT CLOSIN
NET PROCEEDS		12,844,500	